

NORTH CAROLINA REAL ESTATE COMMISSION



ADVISORY COMMITTEE

2004 VACATION RENTAL

REPORT

June 16, 2004

NORTH CAROLINA REAL ESTATE COMMISSION
2004 VACATION RENTAL ADVISORY COMMITTEE

CONTENTS

Committee Members

Background and Recommendations

Meeting #1 Report

Meeting #2 Report

Meeting #3 Report

Exhibits

#1 Vacation Rental Managers Association January 7, 2004 Letter

#2 North Carolina Vacation Rental Act

NORTH CAROLINA REAL ESTATE COMMISSION

2004 VACATION RENTAL ADVISORY COMMITTEE

Members

Melvin L. (Skip) Alston
S&J Management Corporation
P.O. Box 20503
Greensboro, NC 27420-0503
Phone: (336) 272-5779
Fax: (336) 379-7945
E-Mail: msa2820@aol.com

Kim J. Johnson
Jenkins Rentals
P.O. Box 1003
Blowing Rock, NC 28605-1003
Phone: (828) 295-9888, ext. 13
Fax: (828) 295-4492
E-Mail: kim@jenkinsrealtors.com

S.R. "Buddy" Rudd, Jr.
Margaret Rudd & Associates, Inc.
210 Country Club Dr.
Oak Island, NC 28465-8315
Phone: (910) 278-6523
Fax: (910) 278-4576
E-Mail: buddyRudd@rudd.com

Timothy M. Cafferty
B&B on the Beach, Inc.
P.O. Box 564
Corolla, NC 27927
Phone: (252) 453-3033, ext. 309
Fax: (252) 453-2318
E-Mail: tim@resortquestouterbanks.com

Timothy W. Midgett
Midgett Realty
P.O. Box 250
Hatteras, NC 27943-0250
Phone: (252) 986-6322
Fax: (252) 986-2745
E-Mail: timm@midgettrealty.com

Barbara Shaw
Assistant Attorney General
N.C. Department of Justice
Consumer Protection Section
P.O. Box 629
Raleigh, NC 27602
Phone: (919) 716-6000
Fax: 716-6050

Linda A. Hess
Sun Realty of Nags Head, Inc.
P.O. Box 1630
Kill Devil Hills, NC 27948
Phone: (252) 441-4402 (ext. 477)
Fax: (252) 449-4111
E-Mail: LindaHess@SunRealtyNC.com

Wanda J. Proffitt
Carolina Mountain Realty, Inc.
51 West Blvd.
Burnsville, NC 28714-2936
Phone: (828) 682-6166
Fax: (828) 682-6168
E-Mail: wanda@carolinamtnrealty.com

Rick Zechini
Director of Regulatory Affairs
N.C. Association of REALTORS®
One Hanover Square, Ste. 1109
421 Fayetteville Street Mall
Raleigh, NC 27601
Phone: (919) 856-9155
Fax: (919) 856-9157
E-Mail: rzechini@ncrealtors.org

J. Alan Holden
Alan Holden Realty
128 Ocean Blvd. W
Holden Beach, NC 28462-5026
Phone: (910) 842-6061
Fax: (910) 842-8292
E-Mail: holden@infoave.net

Bill Rowe
N.C. Justice & Community
Development Center
P.O. Box 28068
Raleigh, NC 27611
Phone: (919) 856-2177
Fax: 856-2175
E-Mail: bill@ncjustice.org

North Carolina Real Estate Commission Staff Advisors

Phillip T. Fisher, Facilitator
Executive Director

Special Deputy Attorney General Thomas R. Miller
Director, Legal Services Division

Miriam J. Baer	Blackwell M. Brodgen, Jr.	Emmet R. Wood
Assistant Director, Legal Services Division	Chief Deputy Legal Counsel	Director of Audits & Investigations

NORTH CAROLINA REAL ESTATE COMMISSION
2004 VACATION RENTAL ADVISORY COMMITTEE

Background and Recommendations

BACKGROUND

At its January 15, 2004 meeting, the North Carolina Real Estate Commission reviewed a January 7 letter [***Exhibit 1***] from Linda A. Hess, President of the North Carolina Vacation Rental Managers Association, requesting the Commission to convene its *Vacation Rental Advisory Committee* to study and make recommendations concerning possible amendments to the North Carolina Vacation Rental Act [***Exhibit 2***]. The Commission agreed to reconvene the committee to consider the items set forth in Ms. Hess' letter and any other related issues of special interest and concern to the Commission.

In addition to the original committee members (J. Alan Holden, Kim J. Johnson, Timothy W. Midgett, Bill Rowe, S.R. "Buddy" Rudd, Jr. and Barbara Shaw) the Commission invited Ms. Hess and Timothy M. Cafferty to become members and the North Carolina Association of REALTORS® to name a member of its staff (Rick Zechini) to serve on the committee. Chairman Dameron also designated Commission members Melvin L. "Skip" Alston and Wanda J. Proffitt to serve on the committee as the Commission's representatives.

The *2004 Vacation Rental Advisory Committee* met in the offices of the Real Estate Commission March 2, April 1 and June 2, 2004 [***Meeting Reports***]. Commission Executive Director Phillip T. Fisher acted as Facilitator for the meetings. Special Deputy Attorney General Thomas R. Miller, Assistant Director of Legal Services Miriam J. Baer, Chief Deputy Legal Counsel Blackwell M. Brogden, Jr. and Director of Audits and Investigations Emmet R. Wood were Commission staff advisors to the committee. Barbara J. Worzalla, Director of National Accounts for Travel Guard International, and Lee Hughes, Vice-President of the Sales Division for CSA Travel Protection, appeared before the committee April 1 to present information and respond to questions concerning travel insurance. Others attending the meetings were Real Estate Commission Chairman Allan R. Dameron and NCAR Director of Governmental Affairs Stephanie M. Simpson (Meeting #1); Ms. Simpson, Outer Banks Association of REALTORS® President R. Stewart Couch, Senate President Pro Tem Marc Basnight's Chief of Staff Rolf Blizzard, and Robert O. Oakes, Jr. of Village Realty (Meeting #2); and John E. Summerton and Jeff Malarney of Twiddy & Company, Mr. Couch, consultant Christopher B. Smith and Lee N. Hughes (Meeting #3).

The committee discussed those items set forth in the North Carolina Vacation Rental Managers Association's letter and other issues related to vacation rental management. After discussion, the committee recommended that the Real Estate Commission:

RECOMMENDATIONS

1 Endorse amending Section 42A-19(a) of the North Carolina Vacation Rental Act ("Act") to provide that a landlord, when conveying property subject to a vacation rental agreement, would not be required to provide to the purchaser the tenant's address until 10 days after transfer of the property (now 10 days after entering the contract of sale); and to provide that the new owner of property would not be required to provide the tenant his/her name, address and other information currently required if there is no change in the vacation rental manager (or the new owner elects not to honor the vacation rental agreement for persons whose rental ends more than 180 days after recordation of the new owner's deed). [*Note: The committee also requested the Commission to state in*

writing that a landlord may, in lieu of providing the purchaser a copy of each vacation rental agreement as required in Section 42A-19, provide only one copy of the agreement for tenants for whom the provisions of the agreement are the same.]

Purpose: To simplify reporting requirements for vacation rental managers and property owners upon the sale of property subject to vacation rental agreements.

2 Endorse amending Section 42A-36 of the Act to impose upon all tenants the same restrictions on seeking rent refunds from the landlord in the event of a mandatory evacuation regardless of whether the tenant occupies the vacation rental property or has not yet taken possession of it when the evacuation is ordered. [*Ms. Shaw dissented; Mrs. Proffitt not present for vote.*]

Purpose: To subject property owners to the same requirements for refunding rent regardless of whether the tenant is forced to leave the owner's property (i.e., possessory tenant) due to a mandatory evacuation order, or is unable to occupy it (non-possessory tenant) due to a mandatory evacuation order.

3 Publish an informational brochure for owners of vacation rental property addressing such subjects as the purchase/sale of vacation rental properties, what constitutes "fit and habitable," security deposits, vacation interruption insurance, rent refunds, and related topics; and that the Commission charge \$.25 per copy for the publication to offset printing and distribution costs.

Purpose: To better inform owners of vacation rental properties regarding the N.C. Vacation Rental Act and related matters of special interest to them.

4 Suggest in writing to the North Carolina Vacation Rental Managers Association that its members obtain copies of a publication on expedited evictions and appeals available through the Administrative Office of the Courts and to review them, if possible, with the Chief District Court Judge in their areas.

Purpose: To better inform magistrates regarding expedited evictions of tenants pursuant to the N.C. Vacation Rental Act.

OTHER

Those members of the committee engaged in vacation rental management stated that, when tenants of vacation rental properties managed by their companies are given the option of paying a non-refundable "security deposit waiver" fee vs. a security deposit to cover any damages they may accidentally cause to the property, the vast majority choose to pay the waiver fee. Ms. Shaw stated that, since security deposit waiver plans were not contemplated in the Vacation Rental Act, she would confer with other members of the Consumer Protection Section of the North Carolina Department of Justice and, if possible, issue an advisory letter to the Real Estate Commission commenting on this alternative to tenant security deposits.

The committee discussed at length whether Section 42A-16 of the Act should be amended to prohibit landlords and vacation rental managers from disbursing advance rents before tenants occupy the property. After discussion (*See esp. April 1 Meeting Report*) and consulting other vacation rental managers in their communities, the committee concluded that there was no consensus in the vacation rental industry on this issue. Therefore, the committee determined that it would not at this time recommend any amendment to the Vacation Rental Act regarding disbursement of advance rents.

NORTH CAROLINA REAL ESTATE COMMISSION
2004 VACATION RENTAL ADVISORY COMMITTEE

March 2, 2004

Raleigh, North Carolina

REPORT

Committee Members Present:

Melvin L. "Skip" Alston (Greensboro)
Timothy M. Cafferty (Corolla)
Linda A. Hess (Kill Devil Hills)
J. Alan Holden (Holden Beach)
Kim J. Johnson (Blowing Rock)
Timothy W. Midgett (Hatteras)
Wanda J. Proffitt (Burnsville)
Bill Rowe (Raleigh)
S.R. "Buddy" Rudd, Jr. (Oak Island)
Barbara Shaw (Raleigh)
Rick Zechini (Raleigh)

Commission Staff Members Present:

Phillip T. Fisher, Executive Director (Facilitator)
Thomas R. Miller, Director of Legal Services
Miriam J. Baer, Assistant Director of Legal Services
Blackwell M. Brogden, Jr., Chief Deputy Legal Counsel
Emmet R. Wood, Director of Audits and Investigations

Others Present:

Allan R. Dameron, Chairman, North Carolina Real Estate Commission
Stephanie M. Simpson, NCAR Director of Governmental Affairs

Welcome

Mr. Fisher welcomed the members [**Item 1**] to the first meeting of the *2004 Vacation Rental Advisory Committee*. Mr. Fisher explained that the committee consisted of six members of the former advisory committee (Mr. Holden, Ms. Johnson, Assistant Attorney General Shaw, Mr. Midgett, Mr. Rowe from the N.C. Justice & Community Development Center, and Mr. Rudd) which met in 1998 and 1999, and five new members named by the Real Estate Commission (Real Estate Commission members Alston and Proffitt, Mr. Cafferty, Ms. Hess, and North Carolina Association of REALTORS® Director of Regulatory Affairs Zechini).

Background

Mr. Fisher stated that the Real Estate Commission formed the first Vacation Rental Advisory Committee in 1998 to discuss and comment on issues pertaining to vacation rental management practices in North Carolina, including the application of the North Carolina Real Estate License Law, Real Estate Commission rules and other state laws to such practices. Mr. Fisher stated that during its four meetings, the committee developed the North Carolina Vacation Rental Act ("Act") which was enacted by the North Carolina General Assembly effective January 1, 2000 [**Item 2**].

Mr. Fisher added that, in response to concerns raised by the North Carolina Vacation Rental Managers Association ("Association"), the Commission re-convened the committee with additional members for the purpose of discussing whether changes should be made to the Vacation Rental Act with regard to the following and other issues:

Advance Rent Refunds

The Association suggested that Section 42A-17(b) of the Act be moved to Section 42A-31 which would require the landlord and real estate broker to refund to the tenant all payments made by the tenant only in the event the landlord or broker cannot provide property which complies with building codes, has safe common areas, safe and functioning facilities and appliances, etc. as described in Section 42A-31. Mr. Miller responded that the operative word in Section 42A-17(b) is "provide" which requires the landlord and broker to refund rents paid by a tenant when they are unable to provide the property in a fit and habitable condition for any reason, including not only physical damage to the property, but regulatory intervention as well (i.e. emergency evacuation). Mr. Miller contrasted this to Section 42A-36 of the Act which addresses the refund of rents to possessory tenants (tenants occupying the property) when a mandatory evacuation is ordered preventing their continued use of the property.

Mr. Cafferty, Ms. Hess and Mr. Midgett related to the committee their experiences in refunding rent to tenants preceding and in the aftermath of the recent Hurricane Isabel which refunds were complicated by the practice

prevalent in their rental market of disbursing advance rents to landlords as permitted in Section 42A-16 of the Act. Some committee members reported that they encountered owners who were reluctant to refund these funds to the rental manager even when a refund was lawfully due. Mrs. Proffitt questioned whether these problems could not have been alleviated if vacation rental managers had instead retained advanced rents in their trust accounts rather than disbursing them to the property owners. Mr. Holden and Ms. Johnson stated that it is not the prevalent practice in their markets for rental managers to disburse advance rents to owners. The committee then discussed the relative advantages and disadvantages of disbursing advance rent to owners.

The primary **advantage** identified was that advance rent provides positive cash flow for owners in the “off season” better enabling them to pay mortgage payments and other expenses associated with the property when the property is not generating income. Because this provides an additional incentive to purchasers of resort property, it, therefore, also benefits real estate brokers and salespersons engaged in the sale of resort property. However, the vacation rental managers on the committee agreed that the benefits of disbursing advance rents to owners have been diluted in recent years due to several factors, including: (1) the trend for persons to purchase resort property as “second homes” rather than for investment; (2) the trend for persons to delay booking their vacation rentals, thus reducing the amount of advance rents paid; and (3) less use of advance rent disbursement as a sales incentive by inexperienced real estate salespersons and brokers who are not aware of this practice. The committee also identified as another possible advantage of disbursing advance rents to owners the fact that it substantially reduces the amount of funds being held by the vacation rental manager which may be subject to unintentional or intentional misuse.

With regard to the **disadvantages** of disbursing advance rent to owners, the committee re-stated the one previously cited; namely, that the funds are less accessible to the vacation rental manager in the event they must be refunded to the tenant.

To assist the committee in its consideration of whether Section 42A-16 of the Act should be amended regarding the disbursement of advance rents to property owners, those committee members (specifically Mr. Cafferty, Ms. Hess and Midgett) from areas where advance rents commonly are disbursed to owners agreed to discuss this issue with their colleagues, clients and real estate agents who specialize in resort sales and to report their findings to the committee at its next meeting.

Travel Insurance

As an extension of its discussion regarding disbursement of advance rents, the committee considered the role of travel insurance providers in compensating possessory and non-possessory tenants whose use of vacation rental property is affected by storms. Pursuant to Section 42A-36 of the Act, a tenant in possession of property when a mandatory evacuation is ordered is entitled to receive from the landlord a prorata refund of rent paid unless the tenant purchased (or refused to purchase) insurance from the landlord or broker which would have compensated the tenant for the rent. Mr. Miller stated that, when a travel insurance provider reimburses a tenant for lost rent, the provider can then seek reimbursement from the broker or landlord to whom the rent was paid. In discussing whether the landlord vs. the tenant should bear the loss of rent paid when a vacation rental property cannot be occupied due to unforeseen circumstances (e.g., a storm), the committee questioned whether the scope of travel insurance coverage could be expanded to cover non-possessory tenants, whether and under what circumstances insurance providers might be willing to waive their subrogation rights, and how insurance providers may be affected if brokers are prohibited from disbursing advance rents to owners. Additionally, the committee wondered whether travel insurance providers were contemplating any changes in the terms and coverage of their policies based upon their recent experiences in North Carolina as a result of Hurricane Isabel.

To assist the committee in its consideration of these issues, the committee requested Mr. Fisher to invite representatives from the two known providers of travel insurance in North Carolina, CSA Travel Protection and Travel Guard International, to meet with the committee at its next meeting.

Sale of Property Subject to Vacation Rental Agreement

The committee discussed Section 42A-19 of the Act which, among other things, requires sellers of property subject to vacation rental agreements to provide the purchaser the name and address of each tenant and a copy of each agreement within ten days following the contract of sale; and requires the new owner to give each tenant his/her name, address and other related information within ten days after the property is transferred.

With regard to sellers providing purchasers the names/addresses and copies of vacation rental agreements for each tenant prior to closing, Mr. Miller stated that it would be satisfactory to provide only one copy of the lease form if the same form was used for all tenants. *The committee recommended that Section 42A-19 be amended, if necessary, to reflect that only one copy of the uniform lease form and each*

tenant's name must be provided to the purchaser within ten days following the contract of sale, and that each tenant's address be provided within ten days following transfer of the property.

With regard to the requirement that the new owner give each tenant the owner's name/address and other information, the committee concluded that this should not be required if the vacation rental manager stays the same or the new owner elects not to honor the vacation rental agreement (for persons whose rental ends more than 180 days after recordation of the new owner's deed); therefore, the committee recommended that Section 42A-19 be further amended accordingly.

Evictions and Appeals

In response to concerns expressed by some committee members that magistrates and district court judges may not be adequately informed concerning Sections 42A-24 and 42A-25 of the Act regarding expedited evictions and appeals of eviction orders, Mr. Miller stated that the Administrative Office of the Courts has developed a very informative publication addressing these issues. He suggested and *the committee concurred that Association members obtain copies of the AOC publication and review them, if possible, with the Chief District Court Judge in their areas.*

The meeting was adjourned at 3:00 p.m. to be reconvened April 1, 2004 at 9:00 a.m. in the Commission office.

Submitted by:

Phillip T. Fisher

Phillip T. Fisher, Facilitator

This 1st day of April, 2004.

NORTH CAROLINA REAL ESTATE COMMISSION
2004 VACATION RENTAL ADVISORY COMMITTEE

April 1, 2004

Raleigh, North Carolina

REPORT

Committee Members Present:

Melvin L. "Skip" Alston (Greensboro)
Timothy M. Cafferty (Corolla)
Linda A. Hess (Kill Devil Hills)
J. Alan Holden (Holden Beach)
Kim J. Johnson (Blowing Rock)
Timothy W. Midgett (Hatteras)
Bill Rowe (Raleigh)
S. R. "Buddy" Rudd, Jr. (Oak Island)
Barbara Shaw (Raleigh)
Rick Zechini (Raleigh)

Commission Staff Members Present:

Phillip T. Fisher, Executive Director (Facilitator)
Thomas R. Miller, Director of Legal Services
Miriam J. Baer, Assistant Director of Legal Services
Blackwell M. Brogden, Jr., Chief Deputy Legal Counsel
Emmet. R. Wood, Director of Audits and Investigations

Others Present:

Stephanie M. Simpson, NCAR Director of Governmental Affairs
R. Stewart Couch, President, Outer Banks Association of REALTORS®
Robert O. Oakes, Jr., Village Realty (Nags Head)
Rolf Blizzard, Chief of Staff, Senate President Pro Tem Marc Basnight

March 2 Meeting Report

The committee reviewed Mr. Fisher's report describing the committee's discussions and actions taken during its March 2 meeting [Item 1]. With regard to the sale of property subject to vacation rental agreements, Mr. Rowe questioned whether the objectives of the committee's recommendations regarding notice to tenants and new owners could not be achieved by statutory interpretation (imputed knowledge theory) rather than statutory amendment. Mr. Miller agreed to explore this and report to the committee at its next meeting. The committee revised that section of the report to insert in the second paragraph the words, "if necessary," following the phrase

"The committee recommended that Section 42A-19 be amended...."

The March 2 committee meeting report was approved by the committee as revised.

Travel Insurance

As requested by the committee at its March 2 meeting, a representative from Travel Guard International followed by a representative from CSA Travel Protection met with the committee to discuss their travel insurance programs and respond to questions from the committee.

Travel Guard International: Barbara J. Worzalla, Director of National Accounts for Travel Guard International, appeared before the committee. Ms. Worzalla stated that 90% of travel insurance claims relate to "trip interruption" where the insured is unable to use the vacation rental as a result of injury, illness or death, as opposed to "weather" related claims where the insured is unable to have access to or must leave a vacation rental property due to weather problems, notably hurricanes. Regarding claims resulting from weather problems, Ms. Worzalla stated that coverage is immediate once a mandatory evacuation order is announced or when severe weather conditions prevent an insured's use of the vacation rental property. Consequently, rents are refunded to insureds occupying the property (i.e., possessory tenants) at the time the order is issued or weather conditions arise and to persons who cancel their vacation plans prior to or after their planned occupancy of the property (i.e., non-possessory tenants) based upon the evacuation order or severe weather conditions.

Ms. Worzalla stated that, when Travel Guard refunds rents to tenants, it reserves the right to seek reimbursement from the party to whom the rent was paid. She added that, although the company did not do so following Hurricane Isabel, it may in the future, especially where the property owner has "lost rent" coverage. She also expressed concern that some tenants may have received rent refunds from both the insurance provider and the property owner or manager.

When asked whether Travel Guard is contemplating changes in its travel insurance coverage, Ms. Worzalla responded that replacement accommodation coverage

may be changed to clarify that coverage does not apply when the insured is afforded a substitute property; that a limit may be placed on the time within which coverage applies following storms; and that insurance premiums for all policies will be 6 ½ % (now 6% for some policies).

With regard to recommendations for changes to North Carolina's Vacation Rental Act, Ms. Worzalla suggested that the premium cap fixed in the Act be increased to 10% (now 8%) consistent with the cost of retail insurance policies.

Ms. Worzalla stated that, despite the fact that Travel Guard experienced higher than anticipated losses last year as a result of Hurricane Isabel, the company plans to continue offering coverage in North Carolina, and she anticipates other companies entering the market.

Mr. Fisher and the committee thanked Ms. Worzalla for her very helpful information.

CSA Travel Protection: Lee Hughes, Vice President of the Sales Division for CSA Travel Protection, appeared before the committee. Mr. Hughes stated that the CSA travel insurance policy is a Defined Peril Policy with "adverse weather" named as one of the defined perils. According to Mr. Hughes, coverage begins when a mandatory evacuation order is issued and ends when it is lifted; however, coverage continues so long as a governmental authority bans access to the property usually due to infrastructure damage (roads, water, sewerage, etc.). He added that the CSA policy addresses travel to the vacation rental and access to the vacation rental property but not habitability of the property. He stated that, as a result of Hurricane Isabel, CSA received 7,600 payable claims exceeding \$5,000,000.

With regard to CSA pursuing its right to subrogation, he stated that the company has never sought funds from North Carolina property owners or managers although it reserves the right to do so in its policy.

When asked whether CSA has changed its policy following Hurricane Isabel or anticipates changes, Mr. Hughes responded that, to discourage tenants from returning to property which they were forced to evacuate, the CSA policy now covers tenants who have four days remaining on their rental (was two days). However, in the future, even if damage to the infrastructure serving the property prevents the property's use by tenants, coverage will end 15 days after the evacuation order is lifted (previously no limitation). He stated that the premium for the CSA travel insurance policy is currently 6% and that any increase would likely significantly reduce the number of purchasers.

With regard to recommendations for changes to North Carolina's Vacation Rental Act, Mr. Hughes suggested

that the Act be amended so that, in addition to possessory tenants, non-possessory tenants would not be entitled to a refund of their rent if they elect not to purchase travel insurance. He also suggested that tenants who do not purchase travel insurance be required to state in writing that they were offered but declined such insurance, and that additional efforts be made to better educate tenants, property owners and managers concerning the provisions of travel insurance policies. He concluded by stating that, in his opinion, North Carolina has the "best set of regulations" in the country governing vacation rentals.

Mr. Fisher and the committee thanked Mr. Hughes for his very helpful information.

Access America: Mr. Fisher stated that, following the committee's previous meeting, another North Carolina travel insurance provider had been identified, Access America. Although there was not sufficient time to include a representative of the company in the committee's April 1 meeting, Mr. Fisher furnished the committee members information received from Access America for their consideration [Item 2].

Advance Rent Refunds

The committee resumed its discussion regarding disbursement of advance rent as permitted in Section 42A-16 of the Vacation Rental Act. As requested by the committee at its previous meeting, Mr. Cafferty, Ms. Hess and Mr. Midgett reported on their discussions of this issue with local real estate brokers and salespersons engaged in resort property rentals and sales. They were joined in their remarks by Stewart Couch, President of the Outer Banks Association of REALTORS®, and Bob Oakes, President of Village Realty in Nags Head. Mr. Cafferty reported on a recent meeting of the Outer Banks Association of REALTORS® where this issue was discussed. He stated that 75 members attended representing 38 different companies engaged in resort rentals and/or sales. Mr. Cafferty stated that, based upon an informal poll taken at the meeting, it appeared that about one-third of company owners favored no change in the Vacation Rental Act, thereby continuing to allow vacation rental managers to disburse advance rents to property owners; one-third favored changing the Act to prohibit the disbursement of advance rents; and one-third favored a compromise, prompted at least in part because of their concern that if they did not, the Act may be changed to prohibit any disbursement of advance rent.

Regarding those firm owners who were in favor of disbursement of advance rent to property owners, the following reasons were given:

1. Advance rents enable property owners to pay mortgage debt and other expenses in connection

with their properties at a time when the properties are not generating income.

2. If owners cannot receive income during the "off season," funds to repair and maintain their properties will not be available to pay to local contractors and service providers who depend upon the money on a year-round basis.
3. Without advance rents, purchasers will be less likely to buy resort property during the "off season."
4. If rental managers cannot disburse advance rents to owners, the accumulation of rents in their trust accounts will frequently exceed the F.D.I.C. maximum of \$100,000 per owner. Mr. Cafferty indicated this would affect as many as 50 owners of properties his firm manages.
5. The Act currently limits the amount of advance rent that can be disbursed to property owners, and this previously-agreed-to compromise adequately protects the interests of tenants in the event their rent must be refunded.

Those vacation rental managers present whose firms disburse advance rent to property owners stated that, of those tenants due rent refunds as a result of Hurricane Isabel, they were unaware of any tenants who did not receive their rent refunds. However, Mr. Holden responded that this might not have been true had Hurricane Isabel been the intensity of a Hurricane Hazel, and that the Vacation Rental Act should contemplate this possibility. Acknowledging the concerns expressed by persons who favor and those who oppose a change in the Act regarding disbursement of advance rents but recognizing the value of achieving consensus among the interested parties if a change in the Act is recommended, the committee discussed various compromises.

The committee discussed requiring property owners to obtain a bond covering any advance rents they receive; however, Mr. Miller and Ms. Shaw stated that the cost of the bond would likely exceed the amount of advance rent received and likely would not be readily available. Mr. Holden proposed that a change prohibiting the disbursement of advance rent be phased in consistent with the committee's previous discussion; namely, that, if the General Assembly were to amend the Act in mid-2004, the amendment would not become effective until January 2006 to afford property owners and managers adequate time to plan for the change. Mr. Rudd suggested that the committee consider no change in the Act with regard to disbursement of advance rent and instead require rental managers to retain a certain amount of advance rent in reserve (e.g., August through November rents) in the

event it becomes necessary to refund the rent to tenants during the predominant storm season. The committee agreed to consider at its next meeting these and any other alternatives to the current provisions regarding disbursement of advance rent in the hope of satisfying the concerns of interested parties.

Consumer Education

In light of Mr. Hughes' comments concerning property owners' and tenants' lack of understanding of the terms, conditions and coverage of travel insurance policies, the committee considered whether it might be helpful to develop and make available to vacation rental managers an informational brochure for distribution to owners and tenants addressing common aspects of vacation rental transactions. Mr. Fisher requested the committee members to bring to their next meeting any questions or topics which they believe would be appropriate for inclusion in such a publication. The committee will then determine whether to recommend that the project be undertaken.

The meeting was adjourned at 3:00 p.m. to be reconvened May 17, 2004 at 9:00 a.m. in the Commission office.

Submitted by:

Phillip T. Fisher

Phillip T. Fisher, Facilitator

This 2nd day of June, 2004.

NORTH CAROLINA REAL ESTATE COMMISSION
2004 VACATION RENTAL ADVISORY COMMITTEE

June 2, 2004

Raleigh, North Carolina

REPORT

Committee Members Present:

Timothy M. Cafferty (Corolla)
Linda A. Hess (Kill Devil Hills)
J. Alan Holden (Holden Beach)
Kim J. Johnson (Blowing Rock)
Timothy W. Midgett (Hatteras)
Wanda J. Proffitt (Burnsville)
S.R. "Buddy" Rudd, Jr. (Oak Island)
Barbara Shaw (Raleigh)
Rick Zechini (Raleigh)

Commission Staff Members Present:

Phillip T. Fisher, Executive Director (Facilitator)
Thomas R. Miller, Director of Legal Services
Miriam J. Baer, Assistant Director of Legal Services
Blackwell M. Brogden, Jr., Chief Deputy Legal Counsel
Emmet R. Wood, Director of Audits and Investigations

Others Present:

John E. Summerton, Twiddy & Co. (Corolla)
Jeff Malarney, Twiddy & Co. (Corolla)
R. Stewart Couch, President, Outer Banks Association of REALTORS®
Christopher B. Smith, Consultant (Raleigh)
Lee N. Hughes, V.P. CSA Travel Protection (San Diego, CA)

April Meeting Report

The committee approved Mr. Fisher's report for the April 1 meeting as presented [**Item 1**].

Vacation Rental Brochure

The committee resumed its discussion (*See April 1 Meeting Report, p. 5*) as to whether it would be helpful to develop and make available to vacation rental managers an informational brochure for distribution to owners and tenants addressing common aspects of vacation rental transactions. The committee members determined that, through materials already furnished by vacation rental managers, tenants are receiving adequate information about their vacation rentals; however, owners of vacation

rental property could benefit from a publication addressing topics of special interest and concern to them.

The members suggested the following subjects for inclusion in the publication: purchase/sale of vacation rental properties, including notification of vacation rental manager; honoring vacation rental agreements; owners' use of property when tenant fails to pay all rent or to occupy the property; satisfying the "fit and habitable" standard; permitted uses of security deposits, payment by credit card, and possibly "security deposit waiver" in lieu of security deposit (See this report, pp. 2-3); "damage" vs. "ordinary wear and tear", and tenant's obligation for damages; vacation interruption insurance; no "deficit spending" by vacation rental manager; and special emphasis on issues related to rent refunds, including mandatory evacuations, cancellation policies, and failure to provide "fit and habitable" premises.

The members suggested that the format for the publication be similar to the Real Estate Commission's *Questions and Answers on: Purchasing Coastal Real Estate in North Carolina* brochure which the members reviewed. The members further agreed that the publication would be more authoritative if published by the Commission and that the Commission should charge \$.25 per copy to offset printing and distribution costs.

The committee recommended that the Real Estate Commission publish an informational brochure for vacation rental owners as previously distributed.

Mr. Fisher stated that, if approved by the Commission, the Commission staff would develop the publication and circulate a draft to the committee members and Real Estate Commission for their review and approval.

"Security Deposit Waiver"

Mr. Fisher stated that, since the committee's previous meeting, he has been made aware of another topic of interest to vacation rental managers; namely, alternatives to tenant security deposits. Mr. Cafferty and other members of the committee stated that tenants of vacation rental properties managed by their companies are given the option of paying either a non-refundable "security deposit waiver" fee or a refundable security deposit to cover any accidental damages to the property caused by

the tenant or the tenant's guests. They stated that, since the non-refundable waiver fee usually involved less money than the typical refundable security deposit and covered up to \$3000 in accidental damage to the property, the vast majority of tenants opt to pay the security deposit waiver fee rather than a security deposit. All vacation rental managers on the committee agreed that this is an extremely popular product among tenants. In addition, property owners favor the security deposit waiver because it often provides more practical protection for their property, and vacation rental managers prefer it because it is easier to account for and administer and is more profitable.

Mr. Lee Hughes, Vice-President for Sales for CSA Travel Protection, who was present in the audience at the meeting, volunteered to appear before the committee to respond to questions about the security deposit waiver plan. Mr. Hughes described two different programs available through his company to firms depending upon their volume of business.

Regarding the program available to firms with higher volumes of business, Mr. Hughes stated that tenants who choose to participate in the plan pay a \$35-\$40 fee to the vacation rental manager which covers the tenant for up to \$3000 accidental damage caused by the tenant or the tenant's guests to the vacation rental property; however, the damage is covered only if the tenant reports it to the vacation rental manager while the tenant is occupying the property. From the fees received, the vacation rental manager (1) deposits a certain portion (e.g., 45%) in a fund to pay for the repair/replacement of damaged property, (2) pays a certain portion (e.g., 20%) to the assigned administrator of the plan, and retains the balance (35%) as an administrative fee. In the event covered damage exceeds a certain percentage (e.g., 65%) of the security deposit fees collected by the vacation rental manager during a given period, the insurance company represented by the assigned administrator reimburses the rental manager for monies paid in excess of that amount up to a maximum amount (e.g., \$1,000,000).

Regarding the plan for firms with a lower volume of business, Mr. Hughes stated that the coverage, terms and conditions, and fees paid by the tenant are the same as the other plan. However, the vacation rental manager deducts the administrative fee (e.g., 30%) from the security deposit waiver fees collected from tenants and remits the balance to the insurance company. The rental company then pays to repair/replace the damaged property, and the insurance company processes the claims and reimburses the rental company.

Mr. Fisher stated that he and Mr. Miller recently met with persons who propose to offer a similar product to tenants.

According to Mr. Fisher, security deposit waiver plans have recently gained attention due to concerns from vacation rental managers as to whether plans currently being used comply with North Carolina's Tenant Security Deposit Act, Vacation Rental Act, and other applicable laws and rules. Ms. Shaw stated that, in response to an inquiry from Mr. Miller, she sent a December 27, 2000 letter to him from the Consumer Protection Section of the Department of Justice commenting on, among other things, whether it is lawful under the Vacation Rental Act for vacation rental managers to offer tenants a choice between paying a tenant security deposit or purchasing an insurance policy covering them for damages caused to the rental property. She stated that her response was predicated on the notion that tenants would be purchasing insurance to cover their risk, but that based upon the description given of plans currently in place, it appears the additional monies paid by tenants are more in the form of rent rather than insurance premiums. Mr. Miller and Ms. Shaw suggested that, to avoid issues under the Tenant Security Deposit Act and complaints from tenants concerning fees added to rent, property owners and managers could simply build the security deposit waiver fee (and trip interruption insurance) into the rent. However, Mr. Zechini expressed concern that tenants would then no longer have the option of choosing between a potentially refundable security deposit and a non-refundable deposit waiver. The vacation rental managers on the committee were concerned that, since these additional funds would be classified as rent, owners would expect to receive them and that it would be necessary to change their computer software accounting programs to accommodate this change.

Ms. Shaw stated that, in light of the committee's discussion and the fact that security deposit waiver plans were not contemplated in the Vacation Rental Act, she would re-examine the issue. Noting that care must be taken not to create unintended consequences with landlord-tenant law as it applies to long-term rentals, she stated that she would confer with others at the Justice Department and, if possible, issue an advisory letter to the Real Estate Commission addressing this matter.

The committee thanked Mr. Hughes for his assistance.

Mandatory Evacuation of Possessory vs. Non-Possessory Tenants

At the request of Ms. Hess, the committee discussed whether Section 42A-36 of the Vacation Rental Act should be amended. Under the current language of the Act, the landlord must refund tenant security monies paid if the landlord cannot provide the property to the tenant because of a mandatory evacuation or other

official intervention which precludes the tenant's access to the property. However, the landlord is relieved of the obligation to refund the rent if the tenant is in possession of the property at the time the evacuation is ordered and the tenant has been offered insurance which would have covered the tenant's loss. If the tenant is offered and declines the insurance, the tenant bears the risk of loss. Ms. Hess and other vacation rental managers on the committee proposed that tenants whose tenancies were not yet possessory be treated like tenants in possession under the current law. Ms. Baer pointed out to the committee that this would shift the risk of loss in such cases to the tenant from the landlord who, being in the vacation rental business, might reasonably be expected to assume this risk. Several vacation rental managers on the committee believed that tenants should assume more risk for events such as severe storms which are beyond anyone's control. They also projected that the impact of this change would be minimal since the vast majority of tenants purchase trip interruption insurance which covers these risks.

After discussion, *the committee recommended that Section 42A-36 of the Vacation Rental Act be amended as previously described to impose upon non-possessory tenants the same restrictions as currently apply to possessory tenants with regard to the refund of rents in the event of mandatory evacuations. [Ms. Shaw dissented; Mrs. Proffitt not present for vote.]*

Advance Rent Refunds

The committee resumed its discussion regarding disbursement of advance rent as permitted in Section 42A-16 of the Vacation Rental Act (*See April 1 Meeting Report, pp. 4-5*). Mrs. Proffitt stated that, though permitted by the Act, she and some other members of the Real Estate Commission have expressed concern regarding the practice of vacation rental managers disbursing advance rent to owners. The committee members recalled that various compromises were discussed at their previous meetings including retaining a certain amount of advance rent in reserve, and phasing-in or delaying a change to facilitate the transition. However, acknowledging that there was no consensus in the vacation rental industry on this issue, the committee determined that it would not at this time recommend any amendment to the Vacation Rental Act regarding the disbursement of advance rents.

Prior Recommendations

Mr. Miller reviewed with the Commission its previous recommendations concerning amendments to Section 42A-19 of the Vacation Rental Act pertaining to the transfer of property subject to a vacation rental agreement.

Regarding the committee's recommendation that a seller of property subject to vacation rentals be permitted

to provide the purchaser a single copy of the vacation rental agreement rather than a copy of each tenant's agreement as currently required, Mr. Miller stated that it would not be necessary to amend the Act to accomplish this provided that the seller also furnishes the purchaser the names, addresses, rents and dates of the tenancies for the tenants who executed the agreement since this would be the constructive equivalent of providing the purchaser a copy of each vacation rental agreement.

Regarding the committee's recommendation that the seller provide the purchaser each tenant's address within ten days following transfer of the property rather than ten days after entering the contract of sale as currently required, Mr. Miller advised that it would be necessary to amend the Act.

Regarding the committee's recommendation that the new owner be relieved of the obligation to notify tenants of the change of ownership in those cases where the new owner retains the seller's vacation rental manager and elects to honor the tenants' rights under their vacation rental agreements, Mr. Miller advised that it would be necessary to amend the Act.

There being no further business to come before the 2004 Vacation Rental Advisory Committee, Mr. Fisher stated that he would prepare the report for committee's June 2 meeting and final committee report for submission to the Real Estate Commission. Mr. Fisher stated that he plans to submit the report to the Commission at its June 16 meeting and will, therefore, circulate a draft to committee members for their review and comments in advance of the meeting.

Thanking the committee members for their valuable service to the Commission, the meeting was adjourned at 2:40 p.m.

Submitted by:

Phillip T. Fisher

Phillip T. Fisher, Facilitator

This 16th day of June, 2004